

Message Text

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ACTION ARA-10

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C O N F I D E N T I A L SECTION 1 OF 2 MONTEVIDEO 3071

JOINT STATE/AID MESSAGE

E.O. 11652: GDS

TAGS: EGEN, UY

SUBJ: ARGENTINE CONCERN OVER ECONOMIC PLIGHT OF
URUGUAY

REF: BUENOS AIRES 7306

1. SUMMARY: EMBASSY APPRECIATES INFORMATION ON VIEWS OF ARGENTINE FOREIGN OFFICE ON ECONOMIC PLIGHT OF URUGUAY. THIS MESSAGE PROVIDES (A) OUR CURRENT ASSESSMENT OF ECONOMIC SITUATION HERE, (B) OUR ESTIMATE OF GOA MOTIVES IN STIMULATING A MORE ACTIVE US ASSISTANCE ROLE, AND (C) INFORMATION ON CURRENT ANDPROPOSED AID ACTIVITIES HERE. END SUMMARY.

2. CURRENT ECONOMIC SITUATION

A. URUGUAY'S ALREADY AILING ECONOMY HAS BEEN FURTHER SERIOUSLY AFFECTED BY THE RISE IN OIL AND OTHER KEYPRICES, THE EEC'S RESTRICIONS ON MEAT IMPORTS AND A DECLINE IN WOOLPRICES. 1974 PROSPECTS ARE CERTAINLY BLEAK--THE CENTRAL BANK NOW ESTIMATES A BOP DEFICIT OF \$120-140 MILLION, A FISCAL DEFICIT OF 20 PERCENT OF
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EXPENDITURES, AND AN INFLATION RATE OF 75-85 PERCENT.

B. URUGUAY HAS NO DOMESTIC ENERGY SOURCES OTHER THAN HYDROPOWER, AND A RELATIVELY HIGH INCOME LEVEL IMPLYING A GREATER DEPENDENCE ON FOSSIL FUELS THAN IN LOWER INCOME COUNTRIES. INDEED URUGUAY'S EARLY ENTRY INTO THE TRANSPORT AGE IS AN ADDITIONAL HANDICAP NOW AS IT SADDLES THE COUNTRY WITH ENERGY INEFFICIENT EQUIPMENT. FOR EXAMPLE, THE OVERLY EXTENDED AND POORLY EQUIPPED RAIL NETWORK DATES FROM THE EARLY PART OF THE CENTURY.

C. IN 1973 PETROLEUM MADE UP 18 PERCENT OF TOTAL IMPORTS, A FIGURE WHICH MUST BE CONSIDERED IN THE CONTEXT OF THIS SMALL ECONOMY'S NATURALLY HEAVY DEPENDENCE ON FOREIGN TRADE. THIS YEAR, DESPITE CONSERVATION EFFORTS AND HIGHER DOMESTIC PRICES, THE OIL IMPORT BILL WILL TRIPLE TO \$150 MILLION, AND TOGETHER WITH BOTH HIGHER PRICES AND A HIGHER VOLUME FOR OTHER IMPORTS, THE TOTAL IMPORT BILL WILL NEARLY DOUBLE TO OVER \$500 MILLION.

D. DESPITE THE EEC RESTRICTIONS, URUGUAY WILL LIKELY EXPORT MORE MEAT THIS YEAR (ESTIMATED 106-120 THOUSAND TONS) THAN IN 1973 (98 THOUSAND TONS) THANKS LARGELY TO INCREASED BRAZILIAN IMPORT. ALTHOUGH PRICES ARE DECLINING NOW, THE AVERAGE VALUE SHOULD BE COMPARABLE TO LAST YEAR. THE VALUE OF TOTAL EXPORTS SHOULD INCREASE BY 10 PERCENT THIS YEAR, SPURRED BY GAINS IN NON-TRADITIONAL EXPORTS. WHILE A HEALTHY GAIN, THIS WILL NOT NEARLY COVER HIGHER IMPORT COSTS. WE CONSIDER THAT EXTERNAL FACTORS MERIT URUGUAY BEING CONSIDERED ONE OF THE MOST SERIOUSLY AFFECTED COUNTRIES IN LATIN AMERICA. URUGUAY'S INTERNAL ECONOMY, NEVER VERY VIGOROUS, HAS HELD UP QUITE WELL UNDER THE IMPACT OF A CREDIT SQUEEZE AND CONTINUING HIGH INFLATION. MANUFACTURING AND RETAIL TRADE ARE SAID TO BE ONLY SLIGHTLY DOWN FROM LAST YEAR AND UNEMPLOYMENT ONLY SLIGHTLY UP. REAL WAGES ARE FALLING MODERATELY AS GOVERNMENT-ORDERED WAGE BOASTS FAIL TO MATCH THE INFLATION; ANOTHER WAGE ADJUSTMENT IS EXPECTED IN NOVEMBER. IN THE IMPORTANT FARM SECTOR, THE CROP OUTLOOK IS GENERALLY GOOD BUT THE HIGH LIVESTOCK POPULATION SUGGESTS THAT SLAUGHTER RATES WILL HAVE TO BE RAISED IN SPITE OF THE POOR MARKET OUTLOOK.

E. WHILE EXTERNAL PROSPECTS WILL LIKELY REMAIN BLEAK THROUGH 1975, THERE ARE NOW SIGNS THAT THE GOV MAY BE IN A CONFIDENTIAL

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BETTER POSITION TO MANAGE THIS DIFFICULT SITUATION THAN EARLIER EXPECTED. A CAPABLE NEW ECONOMY AND FINANCE MINISTER, ALEJANDRO VEGH VILLEGAS, HAS BEGUN A DRAMATIC PROGRAM OF ECONOMIC LIBERALIZATION WHICH IF IT PROSPERS, COULD MERIT SIGNIFICANT IMF AND IBRD ASSISTANCE. HIS RECENT MOVES TO FREE THE FINANCIAL FOREIGN EXCHANGE MARKET, PERMIT FREE CONVERTIBILITY THEREIN AND TO RAISE INTEREST RATES COULD SPUR THE BEGINNING OF A CAPITAL MARKET HERE WHICH COULD ATTRACT IN-

CREASING AMOUNTS OF CAPITAL FROM ARGENTINA AND OTHER NEIGHBORING COUNTRIES. IN ADDITION, HE HAS BEEN AUTHORIZED TO PLEDGE A PORTION OF THE COUNTRY'S GOLD RESERVES TO HELP DEAL WITH THE BALANCE OF PAYMENTS CRISIS. THE GOU IS ALSO PLANNING TO ISSUE UP TO \$300 MILLION IN DOLLAR BONDS, A PORTION OF WHICH WILL BE MARKETING ABROAD. DEBT RESCHEDULING NEGOTIATIONS FOR SHORT-TERM CREDITS ARE NOW UNDERWAY WHICH SHOULD ALSO HELP ALLEVIATE THE BOP SITUATION. FINALLY THE GOU WILL HAVE RECEIVED \$50 MILLION FROM THE IMF OIL FACILITY BY THE END OF THE YEAR.

F. ALL OF THE ABOVE INDICATES THAT DESPITE VERY SERIOUS ECONOMIC DIFFICULTIES WHICH NOW EXIST AND WILL CONTINUE FOR SOME TIME, THE GOU IS ADOPTING THE APPROPRIATE POLICIES AND TRYING TO MOBILIZE EXTERNAL ASSISTANCE TO HELP MANAGE THE SITUATION.

3. GOA INTEREST

A. ARGENTINA AND BRAZIL HAVE BOTH BEEN FORTHCOMING IN ECONOMIC ASSISTANCE TO URUGUAY THIS YEAR. BRAZIL, IN ADDITION TO BECOMING THE BIGGEST MARKET FOR MEAT EXPORTS, HAS PROVIDED \$15 MILLION MORE TRADE CREDIT ON FAVORABLE TERMS. WE UNDERSTAND THAT NEGOTIATIONS ARE UNDERWAY WITH BRAZIL FOR CAPITAL GOODS CREDITS AND PERHAPS TRADE CONCESSIONS. POTENTIALLY MORE IMPORTANT ARE THE BENEFITS RECEIVED FROM ARGENTINA. APART FROM THE ONGOING JOINT HYDROELECTRIC AND INTERNATIONAL BRIDGE PROJECTS WITH URUGUAY, A COMPREHENSIVE TRADE AGREEMENT POTENTIALLY BENEFICIAL TO URUGUAY HAS BEEN SIGNED AND A \$50 MILLION CREDIT FACILITY ESTABLISHED TO FINANCE URUGUAYAN PURCHASES OF ARGENTINE CAPITAL GOODS. SEVERAL OTHER COOPERATION

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AGREEMENTS HAVE BEEN REACHED. THE SIGNIFICANCE OF THE ARGENTINE TRADE AGREEMENT WILL BECOME CLEARER WHEN THE COUNTRIES AGREE LATER THIS YEAR ON A LIST OF PRODUCTS TO BE EXCLUDED. GIVEN URUGUAY'S INEFFICIENT INDUSTRY, A FAVORABLE DISPOSITION BY ARGENTINA TO KEEP THE LIST SHORT WILL BE IMPORTANT.

B. IN RESPECT TO GOA CONCERN FOR URUGUAY'S ECONOMIC PLIGHT, WE HAVE MAINTAINED INTIMATE CONTACT WITH AMB. DE LA PLAZA, WHOSE LONG FRIENDSHIP FOR URUGUAY IS WELL KNOWN AND WHOSE EFFORTS TO SPUR MORE ACTIVE US SUPPORT FOR THE BORDABERRY ADMINISTRATION, WHILE MERITED, ALSO LIKELY RESPONDS TO GOA

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INTERESTS IN NOT APPEARING TO BE THE MOST IMPORTANT BENEFACITOR OF URUGUAY. MANY URUGUAYANS ARE STILL APPREHENSIVE OF THE ARGENTINE "BEAR HUG" AND STRONGER US SUPPORT TO URUGUAY WOULD HELP BALANCE WHAT MIGHT OTHERWISE APPEAR TO BE EXCESSIVE ARGENTINE/BRAZILIAN COMPETITION FOR INFLUENCE IN URUGUAY. ALSO TO THE EXTENT THE GOB HAS DOUBTS ABOUT THE EFFECTIVENESS OF THE BORDABERRY ADMINISTRATION, STRONGER US SUPPORT FOR THE GOU WOULD SERVE GOA POLICY INTERESTS.

4. USG ASSISTANCE ROLE IN URUGUAY

A. SINCE WW II, THE USG HAS PROVIDED SOME \$317 MILLION IN DIRECT BILATERAL AND INDIRECT (MULTILATERAL CONTRIBUTIONS) ECONOMIC AND MILITARY ASSISTANCE TO URUGUAY. THE PRINCIPAL MULTILATERAL AGENCIES, IMF, IBRD, IDB, OAS AND UNDP ARE ALL ACTIVE HERE AND THE PRESENT AID PROGRAM IS GEARED TO A RATIONAL DIVISION OF LABOR WITH THESE AGENCIES AND TO PROVIDE ASSISTANCE THAT CONFORMS TO GOU AND AID PRIORITIES. ACCORDINGLY, THE AID PROGRAM IN URUGUAY EMPHASIZES AGRICULTURAL DEVELOPMENT, ADVISORY SERVICES AND TRAINING ASSISTANCE IN THE AREA OF ECONOMIC POLICY, AND TAX ADMINISTRATION. USAID/URUGUAY IS PLANNING TWO FY 1975 LOANS IN AGRICULTURE. (AGRICULTURAL RESEARCH AND EXTENSION LOAN, \$4.9 MILLION, AND AN AGRICULTURAL

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CO-OP DEVELOPMENT LOAN

9 \$1.5 MILLION) IN ADDITION, THE GOU

APPEARS INTERESTED IN A CAPITAL GOODS IMPORT LOAN FOR EXPORT-ORIENTED INDUSTRIES (\$15 MILLION) WHICH AID/W HAS TENTATIVELY BUDGETED FOR FY 1976 AUTHORIZATON

B. THIS MISSION CONSIDERS THAT IN VIEW OF THE SERIOUS-NESS OF URUGUAY'S ECONOMIC PLIGHT OVER THE NEXT FEW YEARS, AND THE SOUND DEVELOPMENT-REFORM ORIENTATION ADOPTED BY THE BORDABERRY ADMINISTRATION, URUGUAY MERITS INCREASED EXTERNAL ASSISTANCE FROM INTERNATIONAL AGENCIES INCLUDING AID. SUCH ASSISTANCE HOWEVER, MUST BE RELATD TO THE GOU'S NEEDS AND PRIORITIES AND US ASSISTANCE, WHILE PSYCHOLOGICALLY IMPORTANT, WILL BE MUCH LESS THAN THAT TO BE PROVIDED BY ARGENTINA, BRAZIL AND THE INTERNATIONAL AGENCIES. BOTH THE GOU AND AID AGREE THAT REQUIREMENTS FOR BOP SUPPORT ARE BEST MET BY THE IMF ANDIBRD AND MINISTER VEGH VILLEGAS IS WELL ALONG IN NEGOTIATING AN ASSISTANCE PACKAGE WITH THESE AGENCIES URUGUAY'S MEDIUM AND LONGER TERM EXTERNAL ASSISTANCE NEEDS FOR DEVELOPMENT ARE PRESENTLY AND WILL CONTINUE TO BE MET THROUGH PROJECT LOANS AND TECHNICAL ASSISTANCE FROM THE INTERNATIONAL AGENCIES AND AID ON THE BASIS OF A COORDINATED DIVISION OF LABOR BETWEEN THEM.
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